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PRICING NEW CROP CORN AND SOYBEANS

Prices for the 2000 crop of corn and soybeans have been in a relatively wide range since mid-March, reflecting changing expectations about spring and summer weather. December 2000 corn futures traded to a high of $2.6425 on March 17 and April 3 and a low of $2.495 on April 28. November 2000 soybean futures traded to a high of $5.815 on May 1 and a low of $5.465 on April 28.

While winter and spring precipitation has been well below normal in some important areas of the midwest, the markets have been reluctant to reflect expectations of significant yield loss. There are some obvious reasons for that, including conflicting reports about both the availability and importance of sub soil moisture; inconsistent weather forecasts; and most importantly, recognition that it is early in the season. Planting progress has been rapid and, in general, the market recognizes that spring weather is not as critical as summer weather in determining average yields. History provides ample evidence that both dry and wet springs can be followed by an average yield either above or below trend. The one consistent factor this year has been a forecast of a growing season with above normal temperatures in much of the U.S. This may be a year when average yield and crop size remain uncertain well into the growing season.

While weather and U.S. crop prospects will dominate price behavior for the next several weeks, other factors will play some role. For corn, the prospects of an ample wheat supply and weak export demand means that wheat may continue to be priced as a feed grain, providing some unexpected competition in the domestic feed market. The outbreak of foot and mouth disease in South Korea has significantly slowed their corn import pace. As of April 20, sales of U.S. corn to South Korea for this marketing year were down 42 percent from the pace of a year ago. On the positive side, recent corn sales have been large, with Japan, Taiwan, and Mexico having larger outstanding purchases than a year ago. Reports suggest China has completed its export sales program for the year. Dryness in some Chinese wheat areas also continues to threaten the size of the 2000 harvest. In addition, domestic corn demand is expected to be generally strong due to increased livestock feeding profitability and perhaps increased ethanol consumption.

For soybeans, oil continues to be the weak link due to large domestic supplies and an abundance of low priced vegetable oil in the world market. Another large South American crop will provide stiff competition for U.S. bean and meal exports through October. On the plus side, Chinese buying will push U.S. soybean exports to a record level this year and a healthy livestock sector suggests strong domestic meal demand.

The early April rally in soybean prices briefly pushed new crop cash prices up to the loan level. Prices then declined below the loan rate for much of April, only to rally again on May 1. The question that still prevails is, “should new crop soybeans be priced below the loan rate?” Those who answer yes, believe that the crop will be large and prices will be much lower at harvest. Those who say no believe there is too much weather risk to price below the loan rate. In addition, if there is a price collapse producers can take the loan deficiency payment at harvest in anticipation of a post-harvest price recovery, much like occurred this year. For now, the latter strategy appears less risky than the former.

For corn, new crop prices have been above the loan rate in most markets since January. Prices above the loan rate force a decision about new crop pricing. A fair amount of pricing has probably occurred with December futures in the $2.55 to $2.60 range. As pointed out last week, a relatively weak basis favors the use of futures or hedged-to-arrive contracts, or at least sales for post-harvest delivery. The strategy of buying at-the-money December put options to price harvest deliveries is still not attractive. With a premium in excess of $.20 per bushel, that strategy establishes a minimum harvest time price just barely above the loan rate in most markets. Buying March put options, even though more expensive, would allow producers to benefit from a significant improvement in the basis expected in December. Buying put options might be augmented by selling out-of-the-money call options. The premium for $3.10 December call options was quoted at $.08 on April 28. Selling those options would reduce the net cost of buying put options, but also establish a maximum price that could be received. Pricing small increments of the expected corn crop in a scale-up fashion may be a prudent strategy. If a large percentage of the crop is priced, some replacement with call options could be considered.

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